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E.O. 12356: DECL: OADR
 TAGS: PREL, EFIN, AR, OREP (BAKER AND MATHIAS)
 SUBJECT: MEETING OF SENATOR MAJORITY LEADER SENATOR
 -- BAKER AND SENATOR MATHIAS WITH CENTRAL BANK
 -- PRESIDENT GARCIA VAZQUEZ

1. CONFIDENTIAL - ENTIRE TEXT.
2. THE FOLLOWING MESSAGE WAS CLEARED BY SENATORS BAKER AND MATHIAS (LIMA 684 NOTAL).
3. IN A FRIENDLY AND OPEN EXCHANGE AT THE CENTRAL BANK ON JANUARY 14, CENTRAL BANK PRESIDENT GARCIA VAZQUEZ AND TWO SENIOR ECONOMISTS SOMMER AND GABA DESCRIBED ARGENTINE ECONOMIC PROBLEMS AND PROGRAMS AND RESPONDED TO QUESTIONS FROM SENATOR BAKER AND SENATOR MATHIAS.
4. IN DESCRIBING THE PROGRAM THE SET OF TARGETS WHICH HAS BEEN MENTIONED BEFORE TO THE EMBASSY AND TO THE TREASURY AND FED WAS REPEATED:
 - REDUCTION OF THE GOVERNMENT SECTOR DEFICIT FROM THE CURRENT 14 PERCENT TO 4 PERCENT BY THE END OF 1984;
 - SHARP REDUCTIONS IN THE MILITARY BUDGET WITH INCREASES IN EXPENDITURES FOR HEALTH, EDUCATION AND HOUSING;
 - MAJOR TAX INCREASES THROUGH BOTH NEW TAXES AND IMPROVED COLLECTIONS;
 - AN INCREASE IN REAL WAGES (AT LEAST AT THE LOWER PAID LEVELS) OF 8 PERCENT DURING 1984;
 - GDP GROWTH IN 1984 OF ABOUT 5 PERCENT;
 - A TIGHT MONEY PROGRAM WITH POSITIVE REAL INTEREST RATES FOR SAVERS, AND A REDUCTION OF THE VELOCITY OF MONETARY CIRCULATION; DIRECTION OF CREDIT TO NEW OR INCREASED PRODUCTION.
5. GARCIA VAZQUEZ ADDED THAT IN THE PAST FEW MONTHS THE DEFICIT HAS ACTUALLY BEEN ABOVE 14 PERCENT BECAUSE THE GOVERNMENT WAS NOT PAYING MANY BILLS AND HE SAID THE DEBT WAS ALSO LARGER THAN HAD PREVIOUSLY BEEN ANNOUNCED BECAUSE ADDITIONAL MILITARY DEBT HAD BEEN FOUND.

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6. ON THE BALANCE OF PAYMENTS, SOMMER SAID THE TRADE SURPLUS FOR 1983, TAKING EXPORTS FOB AND IMPORTS CIF, WOULD BE ABOUT 3.3 BILLION DOLLARS BUT INTEREST ON THE DEBT WAS ABOUT 5.3 BILLION LEAVING 2.0 BILLION FOR NEW FINANCING. BOTH EXPORTS AND IMPORTS ARE EXPECTED TO INCREASE MODESTLY IN 1984, BUT THE TRADE SURPLUS SHOULD BE ABOUT THE SAME. TO GET REAL LONG-TERM GROWTH GOING A GREATER INCREASE IN IMPORTS IS NEEDED BUT THAT WOULD REQUIRE INCREASED NEW FINANCING. ARREARS AT THE END OF 1983 WERE ABOUT 2.5 BILLION DOLLARS.

7. IN RESPONSE TO SENATOR BAKER'S QUESTIONS, IT WAS EXPLAINED THAT THERE WERE THREE MARKETS FOR CREDIT IN ARGENTINA. THE OFFICIAL MARKET IN THE BANKING SYSTEM WAS CONTROLLED BY THE CENTRAL BANK AND IN 1983 OFFERED NEGATIVE REAL INTEREST RATES BUT LITTLE NEW CREDIT. THERE WAS ALSO A FREE MARKET OR INTERCOMPANY LOAN MARKET IN WHICH INTEREST RATES WERE MUCH HIGHER AND POSITIVE. FINALLY, THERE IS A SMALL INDEXED SYSTEM IN THE BANKING SYSTEM WHERE LOANS AND DEPOSITS ARE INDEXED TO INFLATION OR TO THE DOLLAR.

8. GARCIA VAZQUEZ SAID IT IS AN IMPORTANT OBJECTIVE OF THE ECONOMIC TEAM TO END THE INDEXATION SYSTEM. AT ANY RATE VARIOUS VARIABLES WILL BE INDEXED TO FUTURE, NOT TO PAST, INFLATION AND A GRADUALLY REDUCING PATTERN OF INFLATION SHOULD THEREBY BE ESTABLISHED WITH INFLATION COMING DOWN FROM 10-11 PERCENT PER MONTH IN JANUARY TO 9-10 IN FEBRUARY, ETC.

9. GARCIA VAZQUEZ COMPLAINED BITTERLY ABOUT CERTAIN CHARGES LEVIED BY THE NEW YORK BANKS WHICH WERE SO UNREASONABLE THAT THEY COULD NOT BE EXPLAINED TO THE ARGENTINE CONGRESS. THE SENATORS POINTED OUT THAT US LEGISLATION HAD ENCOURAGED US BANKERS TO BE MORE REASONABLE ON CHARGES.

10. THE CENTRAL BANK PRESIDENT ALSO SAID THE ARGENTINES HOPE TO DEVELOP SOME SCHEME IN WHICH PAYMENTS OF INTEREST AND PERHAPS EVENTUALLY PRINCIPAL ON THE DEBT WILL BE RELATED TO EXPORT EARNINGS. UNDER SUCH A SCHEME, WHEN EXPORT EARNINGS INCREASED, MORE WOULD BE PAID TO THE BANKS BUT, SHOULD EXPORT EARNINGS FALL, LESS PAYMENT WOULD BE REQUIRED. THE SENATORS INDICATED THAT THEY THOUGHT THE BANKS WOULD HAVE GREAT DIFFICULTY WITH

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SUCH A SCHEME.

11. SENATOR MATHIAS SAID THAT THE SENATE INTERNATIONAL ECONOMIC POLICY COMMITTEE, OF WHICH HE IS CHAIRMAN, WOULD LIKE TO STAY IN TOUCH WITH THE ARGENTINE SITUATION AND BE HELPFUL IF IT COULD BE. HE SUGGESTED THE ARGENTINE AMBASSADOR IN WASHINGTON KEEP THEM INFORMED. ORTIZ
END OF MESSAGE

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